COMMONWEALTH OF PENNSYLVANIA
OFFICE OF ATTORNEY GENERAL

January 26, 1993

ERNEST D. PREATE, Jr.
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Reply To:

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VIA EXPRESS MAIL

Office of the Secretary
Federal Communications Commission
Washington, D.C. 20554

Re: In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation, MM Docket No. 92-266

Gentlemen:

I enclose the original and nine copies of the Comments of the Attorneys General of Pennsylvania, Massachusetts, New York, Ohio and Texas for filing in the above-referenced matter.

Very truly yours,

David R. Weyl

David R. Weyl
Deputy Attorney General
Antitrust Section

DRW/dmh/fccrates.ltr

Enclosures

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

JAN 27 1993

In the Matter of	)	
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Implementation of Sections of the	)	
Cable Television Consumer Protection	)	MM Docket No. 92-266
and Competition Act of 1992	)	
	)	
Rate Regulation	)	

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JAN 27 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

COMMENTS OF THE ATTORNEYS GENERAL OF PENNSYLVANIA, MASSACHUSETTS, NEW YORK, OHIO AND TEXAS

I. Introduction and Summary

The Attorneys General of Pennsylvania, Massachusetts, New York, Ohio and Texas ("the States") submit the following comments to the Commission concerning its Notice of Proposed Rulemaking on Rate Regulation ("Notice") issued pursuant to the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act").[1]

The states have observed throughout the course of their investigation that most cable systems in the United States face little or no competition. As a result, the States have heard numerous complaints about cable rate increases since 1986. It is evident that the Congress received similar complaints, and, as a

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[1]Representatives of the Offices of Attorney General of the five states submitting those comments are among the several members of the Cable Television Investigative Group ("CTIG") specially appointed by the National Association of Attorneys General ("NAAG") Multistate Antitrust Task Force. The CTIG has been actively investigating the cable television industry since 1988. The views in these comments represent the views of the five Offices of Attorney General submitting them, and have not been reviewed, or concurred in, by NAAG, any Office of Attorney General of any other state, or any other government entity or agency.

result, has mandated that cable systems not subject to effective competition be subjected to rate regulation.[2]

In its Notice, the Commission suggested several alternative forms of rate regulation for basic cable service. The States believe that using a "benchmark" system will best accomplish the goals of the 1992 Cable Act. Whatever methodology is ultimately selected by the Commission, it should conform to the following three principles: first, avoid adopting prices that lock-in rates already inflated by monopoly power; second, avoid giving cable operators incentives to strip down basic service; and third, create incentives for cable operators to hold down their costs. In addition, any benchmark employed by the Commission should be simple to administer and should reflect the rates for basic cable service that would be charged in a truly competitive environment. Based on these overriding considerations, the States believe that the benchmark should be based upon rates charged by cable operators facing head to head competition from other cable operators.

Genuinely competitive pricing has been observed only in areas where two or more cable operators have competed directly for customers. Moreover, because there are few such areas in the

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[2]H.R. Rep. No. 852, 102d Cong., 2d Sess., Cong. Rec. H 8323-4 (daily ed. 09/14/92). The States believe that the emergence of effective competition will serve consumers best. Nevertheless, consumers should be granted some rate relief while that competition develops.

United States, the data needed to develop the proper benchmark rates will be relatively easy to collect.

Other benchmarks suggested by the Commission contain serious flaws. The average cable rates charged in 1986 would not be an appropriate benchmark because there is no evidence that 1986 cable rates reflected genuine competition. Similarly, the 1992 cable rates should not constitute the benchmark because, as Congress has observed, cable operators have used their market power to impose huge rate increases in the past few years, and using 1992 rates as a benchmark would enshrine the current excessive rates to the detriment of consumers.

II. Any Benchmark Adopted by the Commission to Guide Rate Setting Should be Linked to Rates Charged Where Cable Companies Compete Head to Head

The Commission seeks comment on a proposal to establish a benchmark rate against which to measure the price of a cable system's basic tier rate. Notice, ¶ 34 et seq. The States agree that a benchmark mechanism of some kind may be an appropriate test for the reasonableness of rates.[3] If a benchmark rate is selected that incorporates the extraordinary price increases that cable operators have imposed on their customers since the passage

[3]Section 623(b)(2)(C) of the 1992 Cable Act directs the Commission to consider several factors in developing a rate regulation mechanism, including rates in areas subject to competition (subsection (i)), direct and common costs (subsections (ii) and (iii)), advertising revenues (subsection (iv)), franchise fees and obligations (subsections (v) and (vi)) and profit (subsection (vii)). The benchmark mechanism proposed here, while relying primarily on subsection (i), could accommodate minor adjustments based on all of the other factors.

of the 1984 Cable Act, however, the Commission's establishment of a benchmark rate will simply perpetuate the unwarranted monopoly profits that the cable industry has enjoyed. As shown below, experience suggests that competitive price discipline exists only where cable companies compete directly with one another, i.e., in situations where one company has overbuilt another company's system, or where multiple overlapping franchises have been awarded and there is actual competition between cable operators in the overlapping franchise areas. For that reason, the States urge that if the Commission adopts a benchmark rate approach, the benchmark rate should be based upon the rates charged by cable operators faced with such direct competition.

Increases of the benchmark rate itself should also be linked to the experience in cable systems that are subject to such direct competition. Since those rates will almost certainly not be regulated by the Commission (See Section 623(a)(2) of the 1992 Cable Act), rates in those areas will present a fair picture of the operation of a genuinely competitive market. The Commission should not adopt Producer Price Index or CPI "escalators" for the benchmark rate. It is reasonable to assume that cable costs, like telephone costs, may actually decline over the next few years;[4] any increases in the benchmark rate should depend upon

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[4]Indeed, the recent activities of both cable companies and telephone companies suggest that from a technological perspective the industries are converging rapidly. See, e.g., Huber, et al., The Geodesic Network II: 1993 Report on Competition in the Telephone Industry (The Geodesic Company 1992) (hereinafter "The Geodesic Network II") at pp. 2.57-2.67.

changes in the competitive price level, not in changes in largely unrelated segments of the economy.

A. The Rates Charged by Cable Operators With Competition From Other Cable Operators Are the Best Indicators of a Genuinely Competitive Rate

Congress has observed the dramatic and disproportionate rate increases imposed by cable operators over the past few years. See, e.g., Section 2(a)(1) of the 1992 Cable Act.

Moreover, these increases do not appear to have been moderated in areas where the alternatives to the incumbent cable operator were limited to other technologies, such as over the air broadcast, MMDS, SMATV, or TVRO.[5]

In one situation, however, the States have observed a significant decrease in the price burdens imposed on consumers. Where a cable operator must compete directly against another cable operator, the rates offered by the cable operator in the area in which it is subject to direct competition are

[5]Under section 623(l)(1) of the 1992 Cable Act, "effective competition" exists only where there is substantial penetration by competing providers of "comparable video programming," or where relatively few households subscribe to cable service. This standard is substantially more rigorous that the definition of "effective competition" found by the Commission in 47 CFR § 76.33 (six broadcast signals available in a cable franchise area constitutes "effective competition").

substantially lower than in near-by markets and in other areas served by the same operators.[6] In Pennsylvania, for example, a survey of cable systems statewide in August, 1991, found that the average price per channel was 55.4 cents per month. In the Allentown metropolitan area, however, where two cable systems compete directly with each other, prices were much lower. One system's rates were 30.9 cents per channel per month; the other system's rates were 33.7 cents per channel per month. The Commission itself found similar pricing disparities in its 1990 Cable Report: Prices for cable systems nationwide averaged 58 cents per channel per month in December, 1989; for overbuilt areas, prices per channel per month averaged 38.2 cents in May, 1990. Report in MM Docket 89-600, 5 FCC Red 4962 (1990), p. 5002, ¶ 67. These data show clearly the impact of competition on rate setting by cable operators, and the benefit to consumers from competitive pricing.

B. Using Rates in Areas Subject to Head to Head Competition as a Benchmark Reduces Administrative Burdens

The use of the rates produced by head to head cable competition as a benchmark is fair, imposes no unusual administrative burdens on the Commission, and is superior to the

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[6]See, e.g., The Geodesic Network II at pp. 5.22-5.24; see, also, FCC Report to Congress, Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service, Dist. No. 89-600 (July 31, 1990), at 41 ("where cable systems compete head to head, per channel rates for basic service are generally significantly lower than the national average").

other benchmark rates proposed by the Commission. First, this benchmark is fair because no cable operator is entitled to profits that exceed levels found to be competitive; in fact, the 1992 Cable Act itself requires that all cable consumers benefit from rates set no higher than rates in areas where there is effective competition. See Section 623(b)(1). If cable operators assert that prices in the selected areas are set below competitive levels, they should come forward and produce evidence to the Commission that this is the case.[7]

Second, the use of this benchmark should not impose any undue burden on the Commission. There are relatively few (perhaps fewer than 100) markets in which there is competition between or among cable companies, and the Commission could gather all of the relevant data within a short period of time. To the extent that cable operators subject to cable competition are insufficiently diverse to permit the application of this benchmark rate directly to all cable companies, the Commission could make reasonable extrapolations from the available data. For example, the Commission could take the data from the selected markets and develop algorithms that could account for variations in homes passed for mile, number of subscribers, number of channels, system age, miles of underground cable, terrain crossed, and above average programming costs. Notice ¶ 37.

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[7]The benchmark rate should be calculated using the rates of both (or all) the cable operators in the areas found to have head to head competition.

The adjustment factor associated with this benchmark would also be relatively easy to calculate. Rather than rely on indices such as the CPI or PPI, or even the SPI proposed by the Commission, the Commission could turn to an index based upon increases in price observed in areas served by competing cable operators.

The States do not support the adoption of the Commission's proposed Service Price Index (SPI). While the SPI attempts to capture increases in prices for many local service items (Notice n. 70) the States do not believe that there is any necessary or even likely correlation between the costs of providing cable service and the cost of providing any of these local services or even a basket of these services. Indeed, there is no reason why in a genuinely competitive market cable prices might not either decline or rise in ways completely unrelated to the performance of these market basket items. Moreover, it would be inconsistent for the Commission to reject cost-based pricing in favor of market prices in setting an initial benchmark, and then base future price increases on a cost-based methodology. If the Commission establishes benchmark rates based on a genuinely

competitive cable market, it should also base increases to those benchmarks on a genuinely competitive cable market.[8]

C. Using Rates in Areas With Head to Head Competition as a Benchmark Is Superior to Other Proposed Benchmarks

The benchmark proposed by the States is superior to other benchmark rate alternatives suggested by the Commission. The States do not support a benchmark based upon rates charged in 1986, before the Cable Communications Policy Act of 1984 prohibited local rate regulation of most cable systems (Notice ¶ 44). Any assumption that rates in 1986 were reasonable because they resulted from a "bidding process" may be unwarranted. Some analysts have suggested that the reasonableness of rates was not always an overriding consideration with respect to granting or withholding franchises.[9] Moreover, the use of 1986 rates would require the Commission to apply an arbitrary adjustment factor to bring those rates to appropriate 1993 levels (See Notice ¶ 45). Rates selected on this basis therefor would likely both be arbitrary in their inception and bear little relationship to the

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[8]If competition develops rapidly (as the Commission is seeking in, inter alia, MM Docket No. 92-265 (Development of Competition and Diversity in Video Programming Distribution and Carriage)), the lifespan of rate regulation may be short. See Section 623(a)(2) of the 1992 Cable Act. For that reason alone, the Commission should favor rate regulation approaches that can be implemented quickly and without the creation of a new regulatory infrastructure.

[9]See e.g., Hazlett, Duopolistic Competition in Cable Television: Implications for Public Policy, 7 Yale Journal on Regulation 65 (1990).

rates in areas subject to competition, which, after all, are the rates clearly preferred under the 1992 Act.

The use of the average rates of cable systems in 1992, proposed by the Commission at Notice ¶ 46, would also fail to achieve the objectives of the 1992 Act. The rates in effect in 1992 on average will almost certainly reflect the cumulative effect of the exercise of monopoly power by cable operators over consumers. The Commission has found that the exercise of monopoly power by cable companies may be pervasive (See Report in MM Docket 89-600, 5 FCC Rcd 4962 (1990), p. 5006, ¶ 76); if that is the case, then using an average of cable rates as a benchmark would simply perpetuate the current excessive prices. Put another way, while such a benchmark would identify which rates were unusually high relative to other cable systems, it would not identify or establish a rate that would have been in effect had there been competition instead of monopoly during the past several years. The Commission itself has recognized this deficiency, Notice ¶ 47, and the States believe that this deficiency is fatal. The Cable Act of 1992, which specifically directs the Commission to replicate the rates that consumers would enjoy as beneficiaries of competition, should not be a vehicle to give implicit blessing to rates that are the end product of years of monopolistic price increases.

III. The Commission Should Prevent Cable Companies from Avoiding Rate Regulation for Historically "Basic Tier" Services

While the States believe that rate regulation for the basic tier of cable services may provide real benefits to consumers, those benefits will be lost quickly if cable operators are permitted to create "bare bones" basic tiers. TCI, the largest MSO, has already begun the process of stripping its basic tier of the most popular "cable" services, leaving only "broadcast stations and franchise-required public, educational and governmental access channels."[10]

In order to avoid this result, the Commission should require, through rules implementing Section 623 of the Act, that cable operators in areas not subject to effective competition be required to offer, as a basic tier subject to rate regulation, a set of services comparable to the basic tier offered by the operator on January 1, 1992. Cable operators would remain free to develop other tiers of service, including tiers with fewer services than the basic tier offered on January 1, 1992 -- but they would not be able to avoid rate regulation of a basic tier of services comparable to the basic tier offered at the time Congress considered, and passed, Section 623.

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[10]See, e.g., letter dated January 19, 1993, from Joshua Noah Koenig to Charles Donaldson (attached hereto as Exhibit A), at p. 1. In New York state, some cable systems not operated by TCI introduced basic broadcast tiers even prior to January 1, 1992.

IV. The Commission Should Permit Effective Enforcement of the Governing Rates

The Commission requests comment on complaint, rate reduction and refund procedures for rates found to be unreasonable. Notice, ¶¶ 97 et seq. The States urge that the Commission be guided by the following principles: First, keep the complaint procedures simple and allow consumers to amend their complaints as many times as necessary; second, levy fines in addition to ordering refunds where violations are found in order to deter abusive practices against consumers; and third, prohibit negative-option marketing practices.

It has been our experience that most consumers will endure a substantial amount of unreasonable conduct from cable operators before they complain. Once they complain, however, consumers often omit relevant facts, with the result that a heavy initial burden of proof will likely result in the rejection of many meritorious complaints. The Commission's rules should recognize the imbalance in legal resources between consumers and cable companies, and should develop appropriately liberal pleading standards.

Second, the Commission has broad authority to order refunds and levy fines under the Communications Act of 1934.[11] Refunds alone, however, are unlikely to ensure broad compliance. The Commission should, therefor, expressly include fines as an

[11] 47 U.S.C. § 501 et seq. § 503 specifically empowers the Commission to seek forfeitures.

available remedy for violations. The severity of fines should be graded according to the number of consumers affected and whether the cable operator or any of its affiliates had previously engaged in similar behavior.

The States have also observed several instances of "negative-option" marketing by cable operators. Typically, a consumer is called by a telemarketing agent early in the morning or at night and asked to try a service free for a month. If the consumer accepts, the service will continue after the first month and the consumer will be billed if no timely call is placed, during business hours, to cancel the service. Such negative-option practices provide a steady flow of complaints to state and local authorities, anger the general public, and should be prohibited by the Commission.

Similarly, when tier changes are made by cable operators, consumers must affirmatively accept or reject such charges that cause their bills to be increased. The Commission should rule that a non-response from a consumer is to be taken as a rejection by the cable operator.

V. Conclusion

The 1992 Cable Act gives the Commission a clear mandate to rein in the excessive prices for basic cable service that have emerged since 1984. The Commission can accomplish this goal by requiring all cable operators in areas not enjoying effective competition to adhere to rates equivalent to the rates charged by

cable operators who compete directly against other cable operators.

Dated: January 26, 1993

Respectfully submitted,

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January 19, 1993

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Subject: TCI of New York, Inc.
Cable Television Service Reconfiguration
and Price Adjustments

Dear Mr. Donaldson:

It was a pleasure to speak with you again on the telephone last week, and to let you know of the plans of our client TCI of New York, Inc. ("TCI"). As promised, we write to you now on behalf of TCI, which operates cable television systems in a number of locations throughout New York, to advise you of its planned reconfiguration of cable television service levels and related TV channel relocations and price adjustments. We are also advising and briefing the State's Commission on Cable Television about this reconfiguration, and we are also providing similar notices to each of the municipalities from which TCI holds cable television franchises.

You are aware, we believe, that on October 5, 1992 Congress enacted into law the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act"). TCI believes that Congress expressed an intent in the 1992 Cable Act that cable companies offer a reasonably priced, entry-level Basic Service consisting of broadcast stations and franchise-required public, educational and governmental access channels. Additionally, customers have told TCI that they also desire a lower-cost, entry-level cable service.

EXHIBIT "A"

In New York, TCI's cable television systems typically offer two levels of service -- Basic, generally consisting of 25 (more or less) channels of programming for approximately $18.00 per month and Expanded Basic (or Plus) consisting of 5 (more or less) channels of programming for $2.50 per month -- for a total price of $20.50 per month for about 30 programming services. Less than 10% of TCI's customers take only the Basic level of service. Both the number of channels and the price for Basic service vary from system to system, depending on broadcast station availability, technical requirements and cost. We have attached a chart describing the various TCI cable TV systems in New York and the specific service prices applicable in each.

Effective as of April 1, 1993, TCI will create an entry-level Basic Service by reconfiguring its two existing levels of service. In a typical example, thirteen channels of programming will be moved from the Basic to the Expanded Basic level of service -- leaving approximately 12 channels (varying in number by system) on Basic and increasing the number of channels on Expanded Basic from about 5 to 18. The monthly price from Basic Service will drop from $18.00 to $10.00 and the price for Expanded Basic will rise from $2.50 to $10.50. The total combined price for the same 30 channels will remain at $20.50 before and after the reconfiguration -- making the service-level reconfiguration neutral in effect from both a programming and a price perspective for those customers who currently take both Basic and Expanded Basic.

We also note that, as of April 1 and as part of the reconfiguration, TCI will also change its current policy respecting one particular program service, American Movie Classics (AMC). This program service will continue to remain available as part of the Expanded Basic level of service (as it is now). However, TCI will no longer extend the previous policy of allowing subscribers to this service level an option to have AMC deleted from their service package for a savings of 25 cents per month. This option will no longer be available, but current subscribers who have taken the option (for a 25 cent discount) will be "grandfathered" and they will not be required to pay a higher price or receive AMC. The "grandfathered" status of these subscribers is subject to change at a future time.

In order to accomplish the described service level reconfiguration, TCI will be repositioning certain program channels on its cable systems (for example, in some systems the ESPN service will be moved from channel no. 8 to channel no. 20). Generally, the programming services on Basic will now be repositioned on channels 2 through 13.

All customers will receive one or more notifications regarding this reconfiguration of service levels and repositioning of programming. The operative assumption is that customers who now are receiving either Basic, or Basic and Expanded Basic, will wish to continue to receive the same level of service they are currently receiving. Therefore, unless a customer explicitly tells TCI that he or she desires to upgrade or downgrade by adding or deleting the Expanded Basic level of service, the customer will continue to receive the service level or levels which that customer received prior to the reconfiguration.

For example, all customers who take Basic and Expanded Basic will continue to receive those two levels of service unless they explicitly indicate that they only wish to receive the Basic level of service. In the case of Basic-only customers, unless they explicitly indicate that they wish to add Expanded Basic (so as not to lose the programming services which are moving from the Basic to the Expanded Basic level of service) they will remain a Basic-only customer. These customers will receive the notices required under law, and an offer to upgrade to Enhanced Basic without payment of any upgrade charge. No Basic-only customer will be upgraded to the Expanded Basic level of service unless the customer affirmatively requests the additional level of service.

TCI's Basic-only customers will have to make a choice: either pay more for more channels or pay less for fewer channels. Of course, once channels are reconfigured, TCI's Basic-only customers will be unable to receive all the programming they now receive unless they are willing to take and pay for the reconfigured Expanded Basic level of service.

In summary, after the reconfiguration of Basic and Expanded Basic services, all customers either will be paying the same total amount for the same number of programming services that they received prior to the reconfiguration or they will be paying less for less services than they received prior to the reconfiguration.

TCI believes, as a matter of past practice, of constitutional law and specific Cable Act language, that it has the right to change the program services offered to customers. TCI has also taken great care to consider the special requirements of New York law, and particularly the provisions of Executive Law section 824-a and the related regulations of the New York State Commission on Cable Television. The proposed service and price reconfiguration would be done in a manner fully consistent with the requirements of those provisions of New York law and regulations. Full disclosure and advance notice will be made to all subscribers, and no upgrade or downgrade charges will be imposed for the exercise of customer options to subscribe to the service level of their choice.

Moreover, TCI has traditionally advised customers of their service and price options and their rights under the law, and it has consistently given fair warning of the possibility of changes in services, service configurations, arrangements and prices. TCI advises its customers, at the time of installation, in paragraph four of its standard Policies and Practices that:

> The services, programming other services, equipment and our charges and rates for them are subject to change. We may, from time to time, rearrange, delete, add or otherwise change programming or services contained in our Basic cable or other services.

Specific programming services may be, and have been added to or deleted from TCI's two most popular levels of service -- Basic and Expanded Basic. The number of channels in each level of service is not constant. Indeed, past practice has demonstrated this fact.

As to TCI's Cable Act rights, except when franchises require a specific number of channels to be carried on Basic service, and then only in circumstances where there is not effective competition, the Cable Act explicitly recognizes a cable TV operator's ability to reconfigure, rearrange or otherwise offer its services as it chooses.

Additionally, TCI makes it a practice to clearly disclose on all marketing pieces and other customer literature which it gives to customers that "Programming, pricing and packages are subject to change."

The reconfiguration described here has been carefully drafted to avoid even the appearance of a "negative option" marketing scheme. We are confident that no violation could be alleged of the New York limits on such "negative option" schemes (section 595.3 of the rules of the Commission on Cable Television), nor of the related provisions of the 1992 federal Cable Act (section 623(f)), which are not effective in any event until April 3, 1993. No customer of TCI will be asked to pay for services to which they have not affirmatively subscribed.

All customers will be given the opportunity to choose the levels of service they want and ample notice of these options. There will be no upgrade or downgrade fees for customers who elect to change their service level. For over 90% of TCI's customers, the changes will be revenue and programming neutral, and no customers will receive a service level or any more services than they had before this reconfiguration unless they specifically ask for it. Significantly, customers will now have a lower-priced option than they had before.

We are also confident that no violation could be alleged of the new federal standards relating to adjustments in subscriber rates and charges (section 623 of the Cable Act). Further, there is language in section 623(h) of the 1992 Cable Act which authorizes the FCC to establish procedures to prevent evasions (including evasions that result from retiering) of the requirement of section 623. TCI believes that a reconfiguration such as it is undertaking does not violate these provisions of the 1992 Cable Act. Because the reconfiguration is both revenue and programming neutral for over 90% of TCI's customers, we believe that the prices for the reconfigured levels of service will fit within the rate regulation presently under consideration by the FCC.

Accordingly, we believe the reconfiguration of Basic and Expanded Basic services complies with Federal law and the laws and regulations of New York.

As soon as customer notification materials are in final form, we will send you a copy for your information. In the meantime, should you have any questions, please do not hesitate to call me at 518-432-1002 to discuss any questions which you may have. At your suggestion, we are sending a copy of this letter to David O. Ward, your colleague in the Department of Law.

Sincerely,

TCI of New York, Inc.

By:

Joshua Noah Koenig
Cohen, Dax, Koenig &
Wiles, P.C.

xc: Hon. Wm. Finneran, Comm. on Cable TV
Mr. Mark Hess, State Manager TCI of NY, Inc.
David O. Ward, Esq., Dept. of Law, Anti-trust